A Report
to the
Montana
Legislature

Financial-Compliance Audit

Department of Revenue

For the Two Fiscal Years Ended June 30, 2016

October 2016

Legislative Audit Division

16-14

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Financial-Compliance Audits

Financial-compliance audits are conducted by the Legislative Audit Division to determine whether an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) licenses.

The Single Audit Act Amendments of 1996 and the Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards require the auditor to issue certain financial, internal control, and compliance reports in addition to those reports required by Government Auditing Standards. This individual agency audit report is not intended to comply with these reporting requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2015, was issued March 29, 2016. The Single Audit Report for the two fiscal years ended June 30, 2017, will be issued by March 31, 2018. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
Room 277, State Capitol
P.O. Box 200802
Helena, MT 59620-0802

Legislative Audit Division
Room 160, State Capitol
P.O. Box 201705
Helena, MT 59620-1705

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LEGISLATIVE AUDIT DIVISION

Angus Maciver, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors:
Cindy Jorgenson
Joe Murray

October 2016

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report on the Department of Revenue for the two fiscal years ended June 30, 2016. Included in this report are two recommendations related to prior year revenue and late property tax distributions.

During the audit we focused our audit efforts primarily on the department's activities related to tax collections and distributions to local governments. The department receives approximately $2 billion dollars each year in taxes, comprised of individual income, corporate, natural resources, and property taxes. Other testing included, but was not limited to, transactions related to liquor, coal taxes, and transfers-in and out. Our audit work included understanding the department's internal control policies and procedures, performing analytical procedures, and reviewing accounting transactions. We also reviewed and tested compliance with selected state laws and department policy.

The department's written response to the audit recommendation is included in the audit report on page C-1. We thank the director and his staff for their cooperation and assistance throughout the audit.

Respectfully submitted,

/s/ Angus Maciver

Angus Maciver
Legislative Auditor

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Appointed and Administrative Officials

Appointed and Administrative Officials

Mike Kadas, Director

Gene Walborn, Deputy Director

Dan Whyte, Chief Legal Counsel

Kristan Barbour, Director, Taxpayer Assistance and Public Outreach

Charles Geary, Director, Human Resources

Ed Caplis, Director, Tax Policy and Research

Lee Baerlocher, Administrator, Business and Income Tax Division

Steve Austin, Administrator, Citizen Services and Resource Management Division

Tim Bottenfield, Director, Information Technology

Shauna Helfert, Administrator, Liquor Control Division

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Montana Legislative Audit Division

Financial-Compliance Audit
Department of Revenue
For the Two Fiscal Years Ended June 30, 2016

October 2016 16-14 Report Summary

The Montana Department of Revenue administers state tax laws by enforcing regulations for more than 38 state taxes and fees. The department collected approximately $2 billion in taxes in fiscal year 2015 and $1.9 billion in fiscal year 2016. Of this, over $203 million was distributed to local governments in fiscal year 2015, and $178 million in fiscal year 2016.

Context

In both fiscal year 2015 and 2016 the Department of Revenue (department) deposited around $1.7 billion of the total tax collections into the General Fund. The main sources of these taxes are listed below.

- Individual Income
- Property
- Natural Resources
- Corporate
- Cigarette & Tobacco
- Liquor/Alcohol
- Lodging Facility
- Retail Telecommunications
- Railroad Car
- Energy
- Contractors Gross Receipts
- Car Rental
- Cement & Gypsum
- Inheritance

In addition to tax administration, the department establishes values for all taxable property. The department also manages unclaimed property, such as abandoned safety deposit boxes, and attempts to return property to its rightful owners. They oversee liquor distribution and licensing operations in the state and administer the eStop licensing program and bad debt collections on behalf of state agencies. The eStop program allows businesses to apply for or renew up to eight state licenses all at once with one payment.

We reviewed the department's internal controls, performed analytical procedures, and reviewed accounting transactions. We also tested the department's compliance with over 140 state laws and regulations.

Results

The report includes two recommendations related to a missing prior year revenue transaction and late reporting of property tax valuations.

As a result of the audit, we issued an unmodified opinion on the department's financial schedules. This means readers can rely on the information presented on the financial schedules.

Recommendation Concurrence	
Concur	2
Partially Concur	0
Do Not Concur	0
Source: Agency audit response included in final report.	

For a complete copy of the report (16-14) or for further information, contact the Legislative Audit Division at 406-444-3122; e-mail to lad@mt.gov; or check the web site at http://leg.mt.gov/audit
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Call toll-free 1-800-222-4446, or e-mail ladhotline@mt.gov.

Chapter I – Introduction

Introduction

We performed a financial-compliance audit of the Department of Revenue (department) for the two fiscal years ended June 30, 2016. The objectives of our audit were to:

1. Determine whether the department's financial schedules present fairly the results of operations and changes in fund equity for each of the fiscal years ended June 30, 2016, and 2015.
2. Obtain an understanding of the department's internal control systems to the extent necessary to support our audit of the department's financial schedules and, if appropriate, make recommendations for improvements in management and internal controls of the department.
3. Determine whether the department complied with selected state laws and regulations during the audit period.
4. Determine the implementation status of prior audit recommendations.

During the audit, we focused our audit effort primarily on tax revenues, distributions to local governments, and liquor and coal tax activities. This included understanding and testing the department's internal control policies and procedures, performing analytical procedures, and reviewing accounting transactions. In addition, we reviewed and tested the department's compliance with over 140 state laws.

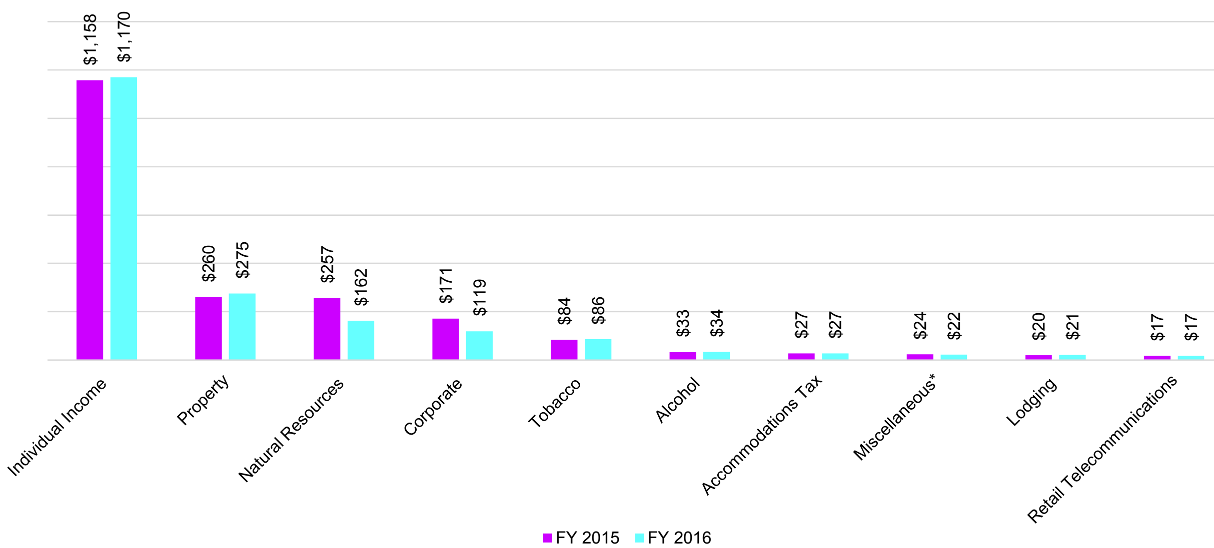
As required by §17-8-101(6), MCA, we analyzed the fees and charges for services and the fund equity of the department's internal service fund, which is used to provide bad debt collection services to state agencies. Bad debt collections primarily occur during the months of January through June when the department is able to offset the debts against requested tax refunds. Due to the timing of the collections, our review noted that at June 30, ending fund equity is around $100,000. The fund equity is spent down from July through December when collections lag and expenditures exceed revenues. Because fees are commensurate with costs for the year as a whole and working capital is not excessive, fund equity is reasonable.

Department Organization and Functions

The department is responsible for the administration of state tax laws and enforcing regulations for numerous state taxes and fees. Revenues collected by the department include, but are not limited to, individual income, corporate income, natural resource, lodging facility use, accommodation, property, alcohol and tobacco taxes. Department tax revenues are recorded primarily in the General, State Special Revenue, and Permanent Funds. Additionally, the department regulates the sale and distribution of alcoholic beverages in the state. The associated taxes are recorded in the Enterprise

Fund. Figure 1 shows the total taxes collected by the department in fiscal years 2015 and 2016 by type.

Figure 1
Taxes by Tax Type
Fiscal Years 2015 and 2016
(in millions)



Source: Compiled by the Legislative Audit Division from State Accounting, Budgeting and Human Resources System records.

*Includes railroad car, energy, contractors gross receipts, car rental consumer counsel, and Public Service Commission taxes.

The department also distributes various tax revenues based on requirements in law. The two largest distributions relate to the local government's entitlement share revenue and oil and natural gas production taxes. The entitlement share is recorded in the Director's Office Program. The oil and natural gas production taxes distributions to counties and school districts are recorded in the Citizen Services & Resource Management Division Program.

For fiscal year 2015-16, the department employed a total of 648.55 full-time equivalent (FTE) employees. The department consists of the Director's Office administering four divisions.

Director's Office (84.75 FTE) provides overall department direction and management. It also supports the agency's director and is composed of the following ten work units:

- Legal Services
- Tax Policy and Research

- Human Resources
- Executive Office
- Office of Taxpayer Assistance
- Information Technology Office
- Enterprise Planning & Analysis Office
- Security Office
- Public Information Office
- Budget and Finance Office

Business and Income Taxes Division (133.45 FTE) administers and collects 38 Montana taxes and fees, oversees tax audits and verifies compliance with Montana tax law for all state taxes, oversees state revenue collection activity, and completes appraisals and assessments of industrial and centrally assessed property.

Citizen Services and Resource Management Division (106.25 FTE) administers the call center, forms design, eStop business licensing coordination, receipt and distribution of unclaimed property, collection of delinquent accounts and return and payment processing. The division provides support services to the department in the areas of accounting, purchasing and facilities, and asset management. The division includes the Financial, Asset Management and Citizen Services Bureau, the Collections Bureau, and the Information Management Bureau.

Liquor Control Division (30.75 FTE) administers the state's Alcoholic Beverage Code, which governs the control, sale, and distribution of alcoholic beverages. The division includes licensing of brokers, manufacturers, wholesalers, importers, and retailers.

Property Assessment Division (293.35 FTE) is responsible for the valuation and assessment of residential, commercial, agricultural, forestland, and business equipment property throughout the state for property tax purposes. The division has a central office located in Helena and four regional offices. There is a local office in each county seat.

Advisory Councils, Boards, and Memberships

The department is a member of the Multistate Tax Commission, the Federation of Tax Administrators, the Western States Association of Tax Administrators, the National Alcohol and Beverage Control Association, the International Association of Assessing Officers, and the National Association of Unclaimed Property Administrators. The department's advisory councils include:

Agricultural Land Valuation Advisory Council is created by §15-7-201(7), MCA, to advise the department concerning the valuation of agricultural property. This council must include a staff member from the Montana State University–Bozeman, College of Agriculture. This advisory council is not a policy making body and has no rule making authority.

Board of Review established in §30-16-302, MCA, and provides policy direction to the department in establishing and operating the eStop business licensing program. The board is attached to the department for administrative purposes only and has separate rule making authority under §30-16-104, MCA.

Forest Land Taxation Advisory Council is created by §15-44-103(10), MCA, to advise the department concerning the valuation of forest land property. The committee consists of seven members, four members with expertise in forest matters, and three members appointed by the governor.

Prior Audit Recommendations

The prior audit for the two fiscal years ended June 30, 2014, contained four recommendations. The department implemented three and partially implemented one.

The partially implemented recommendation relates to assessing Contractor's Gross Receipts tax penalties and interest per §15-50-308, MCA. The audit found that while the department has started to assess penalties and interest, they are still in the process of reviewing all late forms. Additionally, state law allows the department to waive interest up to $100. In the process of implementing the recommendation, the department allowed an additional grace period and waived more than $100 in interest for one of the forms we reviewed. Lastly, when penalty and interest is assessed, the department is required to mail a letter to the person owing the assessment. The letter must advise that if payment is not made, a warrant for distraint may be filed. The department sent out letters when they assessed penalties and interest, but the letter did not include the required advisement language. The department indicated they rarely, if ever, file a warrant for distraint, but plan to update the letter.

Since the department has implemented procedures for reviewing forms to determine if penalty and interest should be assessed, and has made some assessments, we make no further recommendation at this time, and will follow-up on this recommendation in the department's next audit.

Chapter II – Findings and Recommendations

Prior Year Tax Revenues

The Department of Revenue (department) omitted an accounting transaction resulting in a $32 million prior year revenue adjustment error on the state's accounting records.

Section 15-36-311, MCA, requires oil and natural gas production taxes to be paid within 60 days of each quarter ending on March 31, June 30, September 30, and December 31. Therefore, the taxes for the final quarter of fiscal year 2015 were due at the end of August 2015.

Because the taxes are earned as of June 30, 2015, the department recorded an accrual to estimate the taxes due in August as required by state accounting policy. The revenue accrual was coded to the program year the accrual was completed for, in this case fiscal year 2015. In fiscal year 2016 the estimated revenue accrual amount was reversed and actual revenues were recorded.

In fiscal year 2016 when the accrual was reversed, it was matched up to the 2015 accrual and recorded as prior year or program year 2015. Since the accrual reversal was classified as prior year revenue, an additional entry was needed so that prior year revenue only reflected the difference between the estimated amount accrued in the prior year and the actual amount collected in the current year. In fiscal year 2016, the additional entry was not made resulting in the prior year revenue line reflecting the accrual reversal only rather than the difference between the revenue accrual and actual revenue.

At fiscal year-end 2016, all oil and natural gas production tax revenue was completely recorded on the state's accounting system. However, $32 million was misclassified between current and prior revenue.

As a result, prior year revenue is understated by $32,284,586 on the state's accounting records and consequently on the Prior Year Revenues & Transfers-In Adjustments line on the fiscal year 2016 Schedule of Total Revenues & Transfers-In. Department personnel noted human error as the reason for not recording this transaction. The department made a correcting entry in fiscal year 2017 and intends to simplify the process going forward.

Recommendation #1

We recommend the Department of Revenue process all accrual-related transactions on the state's accounting system in accordance with state accounting policy.

Property Tax

The department was late in providing property tax documents required by state law to around 20 percent of the counties.

Section 15-10-202, MCA, requires the department to certify to each taxing authority the total taxable value within the jurisdiction of the taxing authority, by the first Monday in August. Our audit found that the department was one to two days late delivering the 2015 Certification of Values to 11 counties. Department staff indicated that 9 of the 11 counties received the certification late as the department was waiting on centrally assessed values, such as for telecommunications. Revisions to centrally assessed values were made for one company's allocations which the department did not receive until Friday, July 31, 2015.

Section 15-10-305(2), MCA, also requires the department to complete the computation of the amount of taxes, fees, and assessments to be levied against property and notify the county clerk and recorder and county treasurer by the second Monday in October. Our audit found that the department was late between one and nine days turning this information over to eight counties. Each county had a unique situation that resulted in the delay of information, such as last minute changes, formatting issues, a new county system, and employee leave.

Property taxes are a key source of revenue for K-12 schools and the universities. Meeting the dates set in law for reporting tax information is key for ensuring property taxes levied are accurate and complete. Department personnel acknowledged their tardiness, but deemed the delays necessary to get the most accurate information to certify tax values which sometimes involves additional exchanges of data with counties that take more time.

Recommendation #2

We recommend the Department of Revenue comply with §15-10-202, MCA, and §15-10-305(2), MCA, by providing tax information to counties by the required deadlines.

Independent Auditor's Report and Department Financial Schedules

LEGISLATIVE AUDIT DIVISION

Angus Maciver, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors:
Cindy Jorgenson
Joe Murray

Independent Auditor's Report

The Legislative Audit Committee
of the Montana State Legislature:

Introduction

We have audited the accompanying Schedules of Changes in Fund Equity & Property Held in Trust, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out of the Department of Revenue for each of the fiscal years ended June 30, 2016, and 2015, and the related notes to the financial schedules.

Management's Responsibility for the Financial Schedules

Management is responsible for the preparation and fair presentation of these financial schedules in accordance with the regulatory format prescribed by the Legislative Audit Committee, based on the transactions posted to the state's accounting system without adjustment; this responsibility includes recording transactions in accordance with state accounting policy; and designing, implementing, and maintaining internal controls relevant to the preparation and fair presentation of the financial schedules that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial schedules based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial schedules. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial schedules, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the department's preparation and fair presentation of the financial schedules in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the department's internal control, and accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as the overall presentation of the financial schedules.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

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Basis for Adverse Opinions on U.S. Generally Accepted Accounting Principles
As described in Note 1, the financial schedules are prepared from the transactions posted to the state's primary accounting system without adjustment, in the regulatory format prescribed by the Legislative Audit Committee. This is a basis of accounting other than accounting principles generally accepted in the United States of America. The financial schedules are not intended to, and do not, report assets, liabilities, and cash flows.

The effects on the financial schedules of the variances between the regulatory basis of accounting described in Note 1 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

Adverse Opinions on U.S. Generally Accepted Accounting Principles
In our opinion, because of the significance of the matter discussed in the "Basis for Adverse Opinions on U.S. Generally Accepted Accounting Principles" paragraph, the financial schedules referred to above do not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of the department as of June 30, 2016, and June 30, 2015, or changes in financial position or cash flows for the years then ended.

Unmodified Opinions on Regulatory Basis of Accounting
In our opinion, the Schedules of Changes in Fund Equity & Property Held in Trust, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out, present fairly, in all material respects, the results of operations and changes in fund equity and property held in trust of the Department of Revenue for each of the fiscal years ended June 30, 2016, and 2015, in conformity with the basis of accounting described in Note 1.

Other Reporting Required by Government Auditing Standards
In accordance with *Government Auditing Standards*, we have also issued our report dated September 22, 2016, on our consideration of the Department of Revenue's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the department's internal control over financial reporting and compliance.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

September 22, 2016

DEPARTMENT OF REVENUE
SCHEDULE OF CHANGES IN FUND EQUITY & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2016

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Agency Fund	Private Purpose Trust Fund	Permanent Fund
FUND EQUITY: July 1, 2015	$ (27,799,054)	$ 28,726,405	$ 0	$ 797,717	$ 1,750,370	$ 2,668,149	$ 98,718	$ 0	$ 1,492,372	$ 1,146,618,283
PROPERTY HELD IN TRUST: July 1, 2015								$ 180,683		
ADDITIONS										
Budgeted Revenues & Transfers-In	1,794,731,891	254,309,436	316,925		9,036,115	119,751,140	140,126			100,202,075
Nonbudgeted Revenues & Transfers-In	1,773,260	4,230,737		1,537,814		1,670,122	1,775		3,630,332	27,250,867
Prior Year Revenues & Transfers-In Adjustments	(3,841,607)	(35,126,060)		(138,724)	(204,397)	(4,393)			1,153	(1,327,070)
Direct Entries to Fund Equity	(1,633,160,873)	(175,999,332)		(1,699,814)	(8,340,235)	(1,210,492)				(1,082,396)
Additions to Property Held in Trust								6,869,734		
Total Additions	159,502,671	47,414,781	316,925	(300,724)	491,482	120,206,377	141,901	6,869,734	3,631,486	125,043,476
REDUCTIONS										
Budgeted Expenditures & Transfers-Out	182,545,667	49,560,398	316,938			118,213,305	130,323			
Nonbudgeted Expenditures & Transfers-Out	(43,038)	33,742				559,630	3,476		3,657,009	55,758,391
Prior Year Expenditures & Transfers-Out Adjustments	3,284	1,110,522				(4,735)			(70)	
Reductions in Property Held in Trust								6,889,542		
Total Reductions	182,505,913	50,704,662	316,938	0	0	118,768,201	133,798	6,889,542	3,656,939	55,758,391
FUND EQUITY: June 30, 2016	$ (50,802,295)	$ 25,436,523	$ (13)	$ 496,993	$ 2,241,852	$ 4,106,326	$ 106,821	$ 0	$ 1,466,919	$ 1,215,903,368
PROPERTY HELD IN TRUST: June 30, 2016								$ 160,874		

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF REVENUE
SCHEDULE OF CHANGES IN FUND EQUITY & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2015

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Agency Fund	Private Purpose Trust Fund	Permanent Fund
FUND EQUITY: July 1, 2014	$ (1,349,437)	$ 36,240,062	$ 0	$ 738,375	$ 1,807,479	$ 4,467,179	$ 187,153	$ 0	$ 4,691,474	$ 1,123,613,195
PROPERTY HELD IN TRUST: July 1, 2014								$ 594,739		
ADDITIONS										
Budgeted Revenues & Transfers-In	1,886,273,226	281,907,785	294,509		9,060,300	116,955,409	177,935			104,640,478
Nonbudgeted Revenues & Transfers-In	1,155,826	2,689,323		2,087,511		(1,165,107)	2,432		1,017,303	(5,520,615)
Prior Year Revenues & Transfers-In Adjustments	571,776	(1,875,295)		75,001	65,371	(174)				(41,521)
Direct Entries to Fund Equity	(1,735,864,901)	(210,070,172)		(2,103,169)	(9,182,782)	(2,546,794)	(91,786)			(1,181,913)
Additions to Property Held in Trust								6,088,485		
Total Additions	152,135,927	72,651,642	294,509	59,343	(57,110)	113,243,334	88,582	6,088,485	1,017,303	97,896,430
REDUCTIONS										
Budgeted Expenditures & Transfers-Out	178,815,908	77,696,851	294,509			114,776,715	175,665			
Nonbudgeted Expenditures & Transfers-Out	37,239	2,310,293				327,419	1,422		4,221,030	74,891,342
Prior Year Expenditures & Transfers-Out Adjustments	(267,603)	158,156				(61,770)	(70)		(4,626)	
Reductions in Property Held in Trust								6,502,542		
Total Reductions	178,585,544	80,165,299	294,509	0	0	115,042,364	177,017	6,502,542	4,216,405	74,891,342
FUND EQUITY: June 30, 2015	$ (27,799,054)	$ 28,726,405	$ 0	$ 797,717	$ 1,750,370	$ 2,668,149	$ 98,718	$ 0	$ 1,492,372	$ 1,146,618,283
PROPERTY HELD IN TRUST: June 30, 2015								$ 180,683		

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF REVENUE
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2016

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Private Purpose Trust Fund	Permanent Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS										
Licenses and Permits	$ 4,807,967	$ 30,651,302				$ 2,289,708				$ 37,748,977
Taxes	1,712,450,009	157,996,089		$ 1,399,089	$ 8,831,717	27,059,800			$ 30,417,937	1,938,154,642
Charges for Services	2,344	14,630,687				8,095	$ 140,126			14,781,252
Investment Earnings	(3,024)							$ 3,582	67,972,187	67,972,745
Fines and Forfeits	5,839					164,093				169,931
Sale of Documents, Merchandise and Property						91,820,702				91,820,702
Grants, Contracts, and Donations	5,963,012	618,188				37,018	1,775	3,627,904		10,247,896
Transfers-in	53,169,512	14,169,372							27,735,747	95,074,631
Federal Indirect Cost Recoveries	47,087									47,087
Miscellaneous	352,934	59,187				37,454				449,575
Federal	15,867,864	5,289,288	$ 316,925							21,474,077
Total Revenues & Transfers-In	1,792,663,544	223,414,112	316,925	1,399,089	8,831,717	121,416,870	141,901	3,631,486	126,125,871	2,277,941,516
Less: Nonbudgeted Revenues & Transfers-In	1,773,260	4,230,737		1,537,814		1,670,122	1,775	3,630,332	27,250,867	40,094,907
Prior Year Revenues & Transfers-In Adjustments	(3,841,607)	(35,126,060)		(138,724)	(204,397)	(4,393)		1,153	(1,327,070)	(40,641,099)
Actual Budgeted Revenues & Transfers-In	1,794,731,891	254,309,436	316,925	0	9,036,115	119,751,140	140,126	0	100,202,075	2,278,487,708
Estimated Revenues & Transfers-In	1,935,781,451	273,720,994	225,001		8,759,100	116,702,791	187,500		102,064,000	2,437,440,837
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ (141,049,560)	$ (19,411,559)	$ 91,924	$ 0	$ 277,015	$ 3,048,349	$ (47,374)	$ 0	$ (1,861,925)	$ (158,953,129)
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS										
Licenses and Permits	$ 12,063	$ (309,560)				$ (289,332)				$ (586,828)
Taxes	(132,115,088)	(977,544)			$ 277,015	1,606,414			$ 3,364,086	(127,845,117)
Charges for Services	(274,766)	(737,120)	$ (1)			4,964	$ (47,374)			(1,054,297)
Investment Earnings	(3,025)	(1)							84,641	81,615
Fines and Forfeits	839					81,273				82,111
Capital Contributions	(77,000)									(77,000)
Sale of Documents, Merchandise and Property						1,645,031				1,645,031
Grants, Contracts, and Donations	1,695,693	14,187								1,709,880
Transfers-in	1,260,314	(14,964,840)							(5,310,653)	(19,015,179)
Federal Indirect Cost Recoveries	(18,330)									(18,330)
Miscellaneous	(4,220,222)	(1)								(4,220,223)
Federal	(7,310,037)	(2,436,679)	91,925							(9,654,792)
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ (141,049,560)	$ (19,411,559)	$ 91,924	$ 0	$ 277,015	$ 3,048,349	$ (47,374)	$ 0	$ (1,861,925)	$ (158,953,129)

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF REVENUE
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2015

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Capital Projects Fund	Enterprise Fund	Internal Service Fund	Private Purpose Trust Fund	Permanent Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS										
Licenses and Permits	$ 4,812,260	$ 33,186,127				$ 2,239,609				$ 40,237,996
Taxes	1,791,901,821	196,249,206		$ 2,162,512	$ 9,125,672	26,421,847			$ 31,885,375	2,057,746,434
Charges for Services	4,187	14,178,553				4,117	$ 177,935			14,364,792
Investment Earnings	(3,300)							$ 2,953	35,371,544	35,371,197
Fines and Forfeits						102,179				102,179
Sale of Documents, Merchandise and Property						86,957,675				86,957,675
Grants, Contracts, and Donations	8,708,764	621,958				35,472	2,432	1,014,350		10,382,976
Transfers-in	54,998,989	29,246,907				3,780			31,821,424	116,071,100
Inception of Lease/Installment Contract	15,190									15,190
Federal Indirect Cost Recoveries	37,831									37,831
Miscellaneous	(21,566)	56,844				25,449				60,726
Federal	27,546,652	9,182,217	$ 294,509							37,023,378
Total Revenues & Transfers-In	1,888,000,828	282,721,813	294,509	2,162,512	9,125,672	115,790,128	180,367	1,017,303	99,078,343	2,398,371,475
Less: Nonbudgeted Revenues & Transfers-In	1,155,826	2,689,323		2,087,511		(1,165,107)	2,432	1,017,303	(5,520,615)	266,674
Prior Year Revenues & Transfers-In Adjustments	571,776	(1,875,295)		75,001	65,371	(174)			(41,521)	(1,204,842)
Actual Budgeted Revenues & Transfers-In	1,886,273,226	281,907,785	294,509	0	9,060,300	116,955,409	177,935	0	104,640,478	2,399,309,643
Estimated Revenues & Transfers-In	1,842,064,041	330,323,663	251,480		8,984,000	114,167,380	184,300		99,755,000	2,395,729,864
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 44,209,185	$ (48,415,878)	$ 43,029	$ 0	$ 76,300	$ 2,788,029	$ (6,365)	$ 0	$ 4,885,478	$ 3,579,779
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS										
Licenses and Permits	$ 206,211	$ 2,079,203				$ (453,491)				$ 1,831,922
Taxes	53,264,926	(45,279,881)			$ 76,300	2,550,347			$ 1,452,644	12,064,336
Charges for Services	(271,508)	(1,249,491)	$ (1)			1,317	$ (6,365)			(1,526,047)
Investment Earnings	(3,301)	(3,570,000)							1,718,362	(1,854,939)
Fines and Forfeits						1,879				1,879
Capital Contributions	(77,000)									(77,000)
Sale of Documents, Merchandise and Property						687,977				687,977
Grants, Contracts, and Donations	4,969,027	(11,972)								4,957,055
Transfers-in	(2,792,655)	299,454							1,714,472	(778,729)
Federal Indirect Cost Recoveries	(18,330)									(18,330)
Miscellaneous	(9,019,612)	(1)								(9,019,613)
Federal	(2,048,572)	(683,191)	43,030							(2,688,732)
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ 44,209,185	$ (48,415,878)	$ 43,029	$ 0	$ 76,300	$ 2,788,029	$ (6,365)	$ 0	$ 4,885,478	$ 3,579,779

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Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF REVENUE
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2016

	Business & Income Taxes Division	Citizen Services & Resource Management Division	Director's Office	Liquor Control Division	Property Assessment Division	Total
PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT						
Personal Services						
Salaries	$ 6,621,817	$ 3,935,977	$ 5,543,412	$ 1,537,349	$ 12,230,943	$ 29,869,498
Employee Benefits	2,560,951	1,753,337	1,839,231	478,993	5,250,563	11,883,075
Personal Services-Other		(72)		37,416		37,344
Total	9,182,769	5,689,242	7,382,642	2,053,758	17,481,506	41,789,917
Operating Expenses						
Other Services	451,004	709,483	3,366,759	108,877	727,040	5,363,163
Supplies & Materials	120,045	137,918	782,202	175,469	398,489	1,614,123
Communications	179,663	974,292	150,584	56,729	456,895	1,818,163
Travel	226,247	18,804	131,262	39,042	194,425	609,780
Rent	257,854	779,429	225,930	449	1,697,143	2,960,804
Utilities				51,325		51,325
Repair & Maintenance	18,131	27,849	2,289,926	50,008	31,569	2,417,483
Other Expenses	188,115	72,396	126,549	646,246	161,103	1,194,410
Goods Purchased For Resale				76,505,715		76,505,715
Total	1,441,059	2,720,170	7,073,213	77,633,861	3,666,664	92,534,967
Equipment & Intangible Assets						
Equipment			477,070	(31,119)	7,964	453,915
Total			477,070	(31,119)	7,964	453,915
Capital Outlay						
Buildings				(39,980)		(39,980)
Other Improvements				39,980		39,980
Total						
Local Assistance						
From State Sources		49,654,528	129,236,950			178,891,479
Total		49,654,528	129,236,950			178,891,479
From Other Sources						
Distrib from Priv Purp Trusts		3,610,539				3,610,539
Total		3,610,539				3,610,539
Transfers-out						
Fund transfers		1,578	268	38,503,181	55,804,791	94,309,817
Total		1,578	268	38,503,181	55,804,791	94,309,817
Debt Service						
Loans				10,408		10,408
Capital Leases			4,459		502	4,960
Installment Purchases					4,003	4,003
Total			4,459	10,408	4,504	19,371
Post Employment Benefits						
Other Post Employment Benefits		5,955		125,469		131,424
Employer Pension Expense		4,730		98,684		103,414
Total		10,685		224,153		234,838
Total Expenditures & Transfers-Out	$ 10,623,828	$ 61,686,743	$ 144,174,602	$ 118,394,240	$ 76,965,430	$ 411,844,842
EXPENDITURES & TRANSFERS-OUT BY FUND						
General Fund	$ 9,630,452	$ 8,040,753	$ 143,687,188		$ 21,147,520	$ 182,505,913
State Special Revenue Fund	677,437	49,862,972	117,111	$ 34,023	13,119	50,704,662
Federal Special Revenue Fund	315,938		1,000			316,938
Enterprise Fund		38,680	369,303	118,360,218		118,768,201
Internal Service Fund		133,798				133,798
Private Purpose Trust Fund		3,610,539			46,400	3,656,939
Permanent Fund					55,758,391	55,758,391
Total Expenditures & Transfers-Out	10,623,828	61,686,743	144,174,602	118,394,240	76,965,430	411,844,842
Less: Nonbudgeted Expenditures & Transfers-Out	(10,056)	3,608,871	(7,815)	593,653	55,784,556	59,969,210
Prior Year Expenditures & Transfers-Out Adjustments	(699)	1,112,429	(675)	(4,735)	2,681	1,109,001
Actual Budgeted Expenditures & Transfers-Out	10,634,583	56,965,442	144,183,092	117,805,322	21,178,192	350,766,631
Budget Authority	11,066,150	115,891,786	144,684,893	140,895,317	21,647,689	434,185,835
Unspent Budget Authority	$ 431,567	$ 58,926,344	$ 501,801	$ 23,089,995	$ 469,497	$ 83,419,204
UNSPENT BUDGET AUTHORITY BY FUND						
General Fund	$ 275,423	$ 261,072	$ 501,801		$ 469,497	$ 1,507,793
State Special Revenue Fund		58,607,247				58,607,247
Federal Special Revenue Fund	156,145					156,145
Enterprise Fund				$ 23,089,995		23,089,995
Internal Service Fund		58,025				58,025
Unspent Budget Authority	$ 431,567	$ 58,926,344	$ 501,801	$ 23,089,995	$ 469,497	$ 83,419,204

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Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF REVENUE
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2015

	Business & Income Taxes Division	Citizen Services & Resource Management Division	Director's Office	Liquor Control Division	Property Assessment Division	Total
PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT						
Personal Services						
Salaries	$ 6,455,078	$ 3,955,451	$ 5,195,585	$ 1,428,449	$ 12,103,066	$ 29,137,630
Employee Benefits	2,440,812	1,624,156	1,675,367	414,578	5,042,509	11,197,423
Personal Services-Other		(3,606)		40,146		36,540
Total	8,895,891	5,576,002	6,870,952	1,883,173	17,145,575	40,371,593
Operating Expenses						
Other Services	488,340	834,165	1,576,201	124,611	713,652	3,736,970
Supplies & Materials	124,330	135,864	776,365	112,690	531,201	1,680,450
Communications	199,816	942,832	175,138	55,722	787,419	2,160,927
Travel	162,333	28,014	131,364	41,508	70,600	433,818
Rent	217,690	761,484	199,317	2,235	1,710,860	2,891,586
Utilities				52,661		52,661
Repair & Maintenance	44,241	100,452	4,230,749	72,735	75,475	4,523,652
Other Expenses	238,026	102,010	286,064	(14,330)	72,506	684,276
Goods Purchased For Resale				74,572,910		74,572,910
Total	1,474,777	2,904,821	7,375,199	75,020,741	3,961,713	90,737,250
Equipment & Intangible Assets						
Equipment			(20,813)	(120,920)	27,574	(114,159)
Capital leases - equipment			12,859			12,859
Total			(7,955)	(120,920)	27,574	(101,300)
Local Assistance						
From State Sources		76,754,013	126,322,819			203,076,832
Total		76,754,013	126,322,819			203,076,832
From Other Sources						
Distrib from Priv Purp Trusts		4,209,453				4,209,453
Total		4,209,453				4,209,453
Transfers-out						
Fund transfers			262	37,673,456	77,147,569	114,821,287
Total			262	37,673,456	77,147,569	114,821,287
Debt Service						
Loans				11,022		11,022
Capital Leases			2,601		502	3,102
Installment Purchases					3,707	3,707
Total			2,601	11,022	4,209	17,831
Post Employment Benefits						
Other Post Employment Benefits		8,437		124,009		132,446
Employer Pension Expense		6,871		100,217		107,089
Total		15,309		224,226		239,535
Total Expenditures & Transfers-Out	$ 10,370,668	$ 89,459,597	$ 140,563,878	$ 114,691,697	$ 98,286,640	$ 453,372,480
EXPENDITURES & TRANSFERS-OUT BY FUND						
General Fund	$ 9,402,983	$ 8,009,222	$ 140,055,004		$ 21,118,334	$ 178,585,544
State Special Revenue Fund	673,176	77,025,928	135,101	$ 61,083	2,270,012	80,165,299
Federal Special Revenue Fund	294,509					294,509
Enterprise Fund		37,977	373,773	114,630,614		115,042,364
Internal Service Fund		177,017				177,017
Private Purpose Trust Fund		4,209,453			6,952	4,216,405
Permanent Fund					74,891,342	74,891,342
Total Expenditures & Transfers-Out	10,370,668	89,459,597	140,563,878	114,691,697	98,286,640	453,372,480
Less: Nonbudgeted Expenditures & Transfers-Out	(1,182)	4,241,713	12,252	388,502	77,147,460	81,788,745
Prior Year Expenditures & Transfers-Out Adjustments	4,170	151,630	(251,872)	(61,770)	(18,071)	(175,912)
Actual Budgeted Expenditures & Transfers-Out	10,367,680	85,066,254	140,803,499	114,364,965	21,157,251	371,759,648
Budget Authority	10,480,680	122,937,199	141,181,439	132,664,293	21,270,603	428,534,214
Unspent Budget Authority	$ 113,000	$ 37,870,946	$ 377,940	$ 18,299,328	$ 113,352	$ 56,774,566
UNSPENT BUDGET AUTHORITY BY FUND						
General Fund	$ 39,809	$ 50,726	$ 375,795		$ 108,621	$ 574,951
State Special Revenue Fund	3,904	37,797,396	2,145		4,731	37,808,176
Federal Special Revenue Fund	69,287					69,287
Enterprise Fund			0	$ 18,299,328		18,299,329
Internal Service Fund		22,824				22,824
Unspent Budget Authority	$ 113,000	$ 37,870,946	$ 377,940	$ 18,299,328	$ 113,352	$ 56,774,566

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-9.

1. Summary of Significant Accounting Policies

Basis of Accounting

The department uses the modified accrual basis of accounting, as defined by state accounting policy, for its Governmental fund category (General, State Special Revenue, Federal Special Revenue, Capital Projects, Debt Service, and Permanent). In applying the modified accrual basis, the department records:

- Revenues when it receives cash or when receipts are realizable, measurable, earned, and available to pay current period liabilities.
- Expenditures for valid obligations when the department incurs the related liability and it is measurable, with the exception of the cost of employees' annual and sick leave. State accounting policy requires the department to record the cost of employees' annual and sick leave when used or paid.

The department uses accrual basis accounting for its Proprietary (Enterprise and Internal Service) and Fiduciary (Private-Purpose Trust and Agency) fund categories. Under the accrual basis, as defined by state accounting policy, the department records revenues in the accounting period when realizable, measurable, and earned, and records expenses in the period incurred when measurable.

Expenditures and expenses may include: entire budgeted service contracts even though the department receives the services in a subsequent fiscal year; goods ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end; and equipment ordered with a purchase order before fiscal year-end.

Basis of Presentation

The financial schedule format was adopted by the Legislative Audit Committee. The financial schedules are prepared from the transactions posted to the state's accounting system without adjustment.

The department uses the following funds:

Governmental Fund Category

- **General Fund** – to account for all financial resources except those required to be accounted for in another fund. The department records various tax receipts in the General Fund. The primary expenditures in the General

Fund include department payroll costs and distribution of the General Fund entitlement share payments to cities and counties.

- **State Special Revenue Fund** – to account for proceeds of specific revenue sources (other than private-purpose trusts or major capital projects) that are legally restricted to expenditures for specific state program purposes. Department State Special Revenue Funds include various earmarked tax accounts.
- **Federal Special Revenue Fund** – to account for activities funded from federal revenue sources. Department Federal Special Revenue Funds relate to the Federal Mineral Royalty Audit Program.
- **Debt Service Fund** – to account for accumulated resources for the payment general long-term debt of principal and interest. The department deposits coal, metal mine, and resource indemnity taxes into this fund type.
- **Capital Projects Fund** – to account for financial resources used for the acquisition or construction of major capital facilities, other than those financed by proprietary funds or trust funds. Coal severance tax and cigarette tax revenues collected by the department in support of the state Long Range Building Program are accounted for in capital project funds.
- **Permanent Fund** – to account for financial resources that are permanently restricted to the extent that only earnings, and not principal, may be used for purposes that support the government's programs. The department uses this fund to account for its activity in the Permanent Coal Trust Fund; the Cultural Trust Fund; the Coal Severance Tax Income and Bond Funds; the Resource Indemnity Trust and Income Funds; the Treasure State Endowment, Income Regional Water System, and Regional Water Income Funds; and the Big Sky Economic Development Funds.

Proprietary Fund Category

- **Internal Service Fund** – to account for the financing of goods or services provided by one department or agency to other departments or agencies of state government or to other governmental entities on a cost-reimbursement basis. The department's Internal Service Fund accounts for bad debt collection activity.
- **Enterprise Fund** – to account for operations (a) financed and operated in a manner similar to private business enterprises, where the Legislature intends that the department finance or recover costs primarily through user charges; (b) where the Legislature has decided that periodic determination of revenues earned, expenses incurred or net income is appropriate; (c) where the activity is financed solely by a pledge of the net revenues from fees and charges of the activity; or (d) when laws or regulations require that the activities' cost of providing services, including capital costs, be recovered with fees and charges rather than with taxes or similar revenues. The department's Enterprise Fund accounts for the Liquor Control Division's administration of the alcoholic beverage code.

Fiduciary Fund Category

- **Private-Purpose Trust Fund** – to account for activity of any trust arrangement not properly reported in a pension fund or an investment trust fund where the principal and income benefit individuals, private organizations, or other governments. Department Private-Purpose Trust Funds are used to account for unclaimed property, escheated property, and unlocated mineral owner interests.
- **Agency Fund** – to account for resources held by the state in a custodial capacity. Agency funds may be used on a limited basis for internal (to the State) clearing account activity, but these must have a zero balance at fiscal year-end. Property Held in Trust, accounts 2504A and 2504B, have a balance at fiscal year-end because bad debts captured during the offset process must be held in a custodial manner for thirty days for debtor notification and appeal. The department agency funds are used as clearing accounts to facilitate the distribution of receipts from the administration of the eStop licensing program, the county collection reports, bad debt collections, dishonored checks, treasury deposit and bank corrections, Automated Clearing House (ACH) collections and reversals, and account receivable activity.

2. General Fund Equity Balance

The negative fund equity balance in the General Fund does not indicate overspent appropriation authority. The department has authority to pay obligations from the statewide General Fund within its appropriation limits. The department expends cash or other assets from the statewide fund when it pays General Fund obligations. The department's outstanding liabilities exceed the assets it placed in the fund, resulting in negative ending General Fund equity balances for each of the fiscal years ended June 30, 2015, and June 30, 2016.

3. Direct Entries to Fund Equity

Direct entries to fund equity in the General, State Special Revenue, Debt Service, Capital Projects, Enterprise, and Permanent funds include entries generated by SABHRS to reflect the flow of resources within individual funds shared by separate agencies. The General Fund also includes adjustments for Insure Montana Tax Credits for previous periods that occurred at least two fiscal years prior. The State Special Revenue Fund includes changes to fund equity designations resulting from an internal review.

4. Revenues Over (Under) Estimate

The Schedule of Total Revenues & Transfers-In for the fiscal year ended June 30, 2015, reports revenues over estimate by $44,209,185 in the General Fund and under estimate by $48,415,878 in the State Special Revenue Fund. In addition, the Schedule

of Total Revenues & Transfers-In for the fiscal year ended June 30, 2016, reports revenues under estimate by $141,049,560 in the General Fund and $19,411,559 in the State Special Revenue Fund. These are explained below:

General Fund – For the fiscal year ended June 30, 2015, income tax was underestimated by approximately $71 million because the assumptions underlying the estimates did not match actual experience. Natural resource tax revenue was less than estimated by approximately $24 million due to a decrease in the price of oil. In addition, actual revenues collected for property tax (95 mills) were $5.8 million less than estimated and corporation license tax revenues collected were $17.8 million more than estimated. A portion of the difference in corporation license tax revenues was attributable to a one-time audit payment of $16.7 million in fiscal year 2015. There was also a $9 million unnecessary revenue estimate established in the miscellaneous receipts account. Finally, telephone license taxes were overestimated by $5.6 million.

For the fiscal year ended June 30, 2016, individual income tax collections were $44.8 million less than estimated because the assumptions underlying the estimates did not match actual experience. Also, a portion of the collections was affected by a retroactive federal tax policy change. The federal law change made it possible for some taxpayers to pay less in fiscal year 2016 than originally estimated. Natural resource tax revenue was lower than estimated by $24.5 million due to a decrease in the price of oil, fluctuating commodity prices, and the closure of a mining operation. The oil price reduction also resulted in a decrease in U. S. Federal Mineral Royalty revenue causing a $7.3 million over estimation. In addition, corporation license tax revenues collected were $61.5 million less than estimated. Decreased estimated payments and an increase in refunds requested by oil and gas companies contributed to a portion of the difference between estimated revenues and collections for corporation tax. There was also a $4.2 million unnecessary revenue estimate established in the miscellaneous receipts account.

State Special Revenue Fund – Revenues in the state special revenue fund were less than estimated for the fiscal year 2015. Natural resource tax revenue was overestimated by $42.7 million due to a decrease in the price of oil. There was also a $3.6 million revenue estimate in an investment earnings account in the Montana Oil and Gas Tax Clearing Fund that was not needed. Finally, bentonite revenue collections were $1.8 million less than estimated.

Revenues in the state special revenue fund were less than estimated for the fiscal year ending June 30, 2016. Natural resource tax revenue was $28.3 million lower than estimated due to a decrease in the price of oil, fluctuating commodity prices, and the

closure of a mining operation. The oil price reduction also resulted in a decrease in U. S. Federal Mineral Royalty revenue causing a $2.4 million over estimation. The Schedule of Total Revenue & Transfers-In includes a $2.9 million revenue estimate in a nonbudgeted transfer account for the Big Sky Economic Development Fund. Revenue transfers to this fund are not included in budgeted revenue collections on the schedule. Also, the Treasure State Endowment Program Funds were established with revenue estimates totaling $12.3 million. However, due to legislative changes, these funds received enough money from the general fund in fiscal year 2015 that a transfer from the permanent funds was not needed in fiscal year 2016. In addition, for the 4th quarter combined oil and gas distribution, revenue were not reclassified to the proper year, which resulted in a $32.3 million entry reported as prior year revenue on the fiscal year 2016 financial statements. The revenue estimate for Public Service Commission Tax was based on total revenue in fiscal year 2014. The fiscal year 2014 tax rate was considerably higher than the tax rate for fiscal year 2016; therefore, the revenue was overestimated by $2 million in fiscal year 2016. Finally, Bentonite Production Tax collections and Accommodations Tax collections were $1.4 million and $1.3 million less than estimated.

5. Nonbudgeted Expenditures and Transfers-out

Nonbudgeted Expenditures and Transfers-Out in the permanent fund, on the Schedule of Changes in Fund Equity & Property Held in Trust, is approximately $75 million for fiscal year 2015 and $56 million in fiscal year 2016. This amount is also reflected on the Schedule of Total Expenditures & Transfers-Out and is related to the coal tax transfers required by state law. These include transfers from the Coal Tax Bond Fund, distributions of investment earnings on the Treasure State Endowment Funds, Big Sky Economic Development Fund, Resource Indemnity Trust Fund and the coal tax trust funds.

6. Unspent Budget Authority

The Schedule of Total Expenditures & Transfers-out for fiscal years 2015 and 2016 report unspent budget authority under the Citizen Services and Resource Management Division of $37,797,396 and $58,607,247 respectively, in the State Special Revenue Fund and $18,299,328 and $23,089,995, respectively, under the Liquor Control Division in the Enterprise Fund.

The unspent budget authority in the Citizen Services and Resource Management Division is created due to fiscal years 2015 and 2016 revenues collected or accrued and distributed to local governments being less than estimated. Fiscal years 2015 and 2016 combined oil and natural gas production tax estimates were created based on

higher natural gas prices and production than were realized. In addition, distributions of bentonite taxes received to Carbon and Carter counties for fiscal years 2015 and 2016 were less than estimated.

The Liquor Control Division receives language appropriations for funds necessary to maintain adequate inventories; pay freight charges; and transfer profits, taxes, and liquor licensing revenues to the appropriate accounts. In fiscal years 2015 and 2016, the appropriation was not to exceed $132.7 million and $140.9 million, respectively. The department purchased inventory and distributed profits and taxes based upon the volume of sales and did not spend up to the total appropriation authority. The language appropriation for the transfer of licensing revenues also includes appropriation authority for both the Department of Revenue and the Department of Justice to administer liquor licensing. By law, the transfer of the licensing revenue is net of the appropriation authority for the Department of Revenue and the Department of Justice and deferred revenues.

7. Prior Year Revenues

On the Schedule of Changes in Fund Equity & Property Held in Trust and the Schedule of Total Revenues & Transfers-In for fiscal year 2015 and 2016, the department recorded transactions that total ($1,875,295) and ($35,126,060) respectively, in the State Special Revenue Fund and ($3,841,607) in fiscal year 2016 in the General Fund as explained below:

- **State Special Revenue Fund** – The majority of the transactions recorded as prior year revenue in the State Special Revenue Fund during fiscal year 2015 represents the difference between the reversal of estimated revenues accrued in the prior year versus current year actual revenue collections reclassified as prior year revenue. The ($35M) prior year revenue balance in fiscal year 2016 is the result of using program year 2015 instead of program year 2016 to record the reclassification of fiscal year 2015 Combined Oil and Gas (COG) clearing revenue received in fiscal year 2016 back to fiscal year 2015. While this creates a misstatement on the department's financial statement, it has no effect on the state's Comprehensive Annual Financial Report (CAFR) which does not differentiate between fiscal years.
- **General Fund** – The majority of this activity includes the difference between reversing estimated revenues accrued in the prior year versus reclassifying current year actual revenue collections as prior year revenues plus the reversal of accounts receivable revenues accrued in the prior year at fiscal year end.

8. Financial Schedules Rounding

The financial schedules for the two fiscal years ended June 30, 2016, do not foot or cross-foot due to rounding. However, the rounding issue is immaterial and the

department considers the schedules an accurate representation of the financial activity reported in SABHRS by the department.

9. Loss Contingencies

The district court has awarded Department of Revenue agency liquor stores $14 million regarding a class action lawsuit related to commission rates. The court decided current statue is unconstitutional and agency stores are entitled to damages as far back as 1995. In addition to the $14 million award, another hearing is scheduled for December regarding attorneys' fees and interest. While some damage amount is reasonably possible, the $14 million is subject to appeal before the Supreme Court.

Report on Internal Control and Compliance

LEGISLATIVE AUDIT DIVISION

Angus Maciver, Legislative Auditor
Deborah F. Butler, Legal Counsel

Deputy Legislative Auditors:
Cindy Jorgenson
Joe Murray

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Schedules Performed in Accordance with *Government Auditing Standards*

The Legislative Audit Committee
of the Montana State Legislature:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the Schedules of Changes in Fund Equity & Property Held in Trust, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out of the Department of Revenue for each of the fiscal years ended June 30, 2016, and 2015, and the related notes to the financial schedules, and have issued our report thereon dated September 22, 2016.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial schedules, we considered the Department of Revenue's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial schedules, but not for the purpose of expressing an opinion on the effectiveness of Department of Revenue's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department of Revenue's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial schedules will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal controls was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify

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any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department of Revenue's financial schedules are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial schedule amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the department's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the department's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

September 22, 2016

Department of Revenue

Department Response

Montana Department of Revenue

Mike Kadas
Director

Steve Bullock
Governor

October 18, 2016

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OCT 20 2016
LEGISLATIVE AUDIT DIV.

Angus Maciver, Legislative Auditor
Legislative Audit Division
Room 160, State Capitol
P O Box 201705
Helena, MT 59620-1705

Dear Mr. Maciver:

Thank you for the opportunity to respond to the Financial-Compliance Audit Report recently completed for the two fiscal years ended June 30, 2016. This audit report includes two recommendations with which the department concurs. Our response to the recommendations is as follows:

Recommendation #1:

We recommend the Department of Revenue process all accrual-related transactions on the state's accounting system in accordance with state accounting policy.

Concur. The department made the necessary correcting journal entry to properly reflect prior year revenues and current year revenues and will simplify the recording of the transactions needed when accruing oil and natural gas production taxes at fiscal year-end.

It is important to note for state financial reporting purposes there is not a misstatement of revenues as the state's Comprehensive Annual Financial Report (CAFR) does not differentiate between current year and prior year revenue. This classification difference is only reflected on the financial statements included in the blue book (financial-compliance) audit of the department. The net effect of the overstatement of current year revenues and the understatement of prior year revenues for state financial reporting purposes is zero.

Recommendation #2:

We recommend the Department of Revenue comply with 15-10-202, MCA, and 15-10-305(2), MCA, by providing tax information to counties by the required deadlines.

Concur. The department acknowledges the delays in the certifications of taxable values. Department records indicate two counties were two days late and nine counties were one day late. The department strives to meet the specific deadline in statute, but also deems it important to have the most accurate information to certify values. This often entails a back and forth exchange of data with the counties. Reasons for the minimal delays included adjustments to levy district allocations, ensuring centrally assessed values that were changing were finalized, capturing newly taxable property within the counties and software issues experienced by some counties. The department continues to work on improving processes between the department and counties. It should be noted certifications were delivered on time for the current year.

Under section 15-10-305, MCA, county clerk and recorders are to deliver the number of mills to be levied within 30 days after receiving certified taxable values. Nineteen counties delivered mills to the department by the deadline and thirty-seven counties delivered mills to the department after their statutory deadline. After the mills are received from the county clerk and recorder, the department is required to compute the amount of taxes, fees, and assessments (tax rolls) by the second Monday in October, plus additional days equal to the number of days the mills were received late. As indicated above pertaining to certification of values, the department strives to meet the specific deadline in statute, but also deems it important to have the most accurate information to complete the tax rolls. Reasons for the minimal delays between the department and counties included waiting to capture data associated with appeals and special improvement districts, system issues encountered when entering and formatting data, and waiting to finalize industrial property changes.

Thank you again for allowing the department to respond to the Financial-Compliance Audit Report and the opportunity to discuss the issues with you and your staff during the exit conference. I also thank your staff who conducted the audit for their professional approach and their fairness in working through the issues as they were raised.

Sincerely,

Mike Kadas
Director